

# LEGISLATIVE RESEARCH COMMISSION

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## INSURANCE REGULATION



REPORT TO THE  
1985 GENERAL ASSEMBLY  
OF NORTH CAROLINA

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December 13, 1984

TO THE MEMBERS OF THE 1985 GENERAL ASSEMBLY:

This is the Legislative Research Commission's report to the 1985 General Assembly on the matter of insurance regulation. This report is made pursuant to Sections 1(3) and 6 of 1983 Session Laws Chapter 905 (HB 1142), was prepared by the Legislative Research Commission's Insurance Study Committee, and is transmitted by the Commission for your consideration.

Respectfully submitted,

*Liston B. Ramsey*  
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Speaker of the House

*W. Craig Lawing*  
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Senate President Pro Tempore

Cochairmen  
Legislative Research Commission



## CONTENTS

	<u>Page</u>
INTRODUCTION .....	1
COMMITTEE ACTIVITY .....	5
COMMITTEE FINDINGS AND RECOMMENDATIONS	
FINANCIAL REGULATION OF INSURANCE COMPANIES	
Forward .....	9
Formation and Organization .....	9
Licensing .....	10
Investments .....	11
Reserves .....	12
Reporting Requirements and Examinations ....	13
Analysis of Financial Statements .....	14
RECOMMENDATION .....	16
INSURANCE HOLDING COMPANY SYSTEMS	
Background .....	19
The NAIC Model Act .....	20
Significance Today .....	21
RECOMMENDATION .....	22
INSURANCE GUARANTY FUNDS	
Background .....	25
The NAIC Model Acts .....	26
North Carolina Legislation .....	27
RECOMMENDATION .....	27

WORKERS' COMPENSATION

Self-Insurance.....	31
Security Fund .....	32
RECOMMENDATION .....	32
INSURANCE STATUTES REWRITE .....	35
RECOMMENDATION .....	39
CONCLUSION .....	41

APPENDIX

- Exhibit A: 1983-84 Legislative Research Commission
- Exhibit B: 1983-84 Insurance Study Committee
- Exhibit C: Letter dated September 14, 1983, from New  
York Senator John R. Dunne to South  
Carolina Representative Warren D. Arthur,  
IV, transmitting the report of the  
Conference of Insurance Legislators' (COIL)  
Task Force on Regulatory Initiative
- Exhibit D: Introduction and Summary (with footnotes) from  
the COIL Report
- Exhibit E: Joint Statement of The Honorable John R.  
Ingram and Mr. Robert Hunter, presented to  
the Committee on September 6, 1984.
- Exhibit F: Statement of Mr. James E. Long presented to  
the Committee on October 3, 1984.
- Exhibit G: Rule V of the North Carolina Industrial  
Commission

Exhibit H: Proposed Legislation: Workers' Compensation  
Self-Insurance Regulation Transfer

Exhibit I: Proposed Legislation: North Carolina  
Insurance Regulation Study Commission





## INTRODUCTION

Many study reports begin with summaries of the recommendations of the study group, and then proceed to describe the information that the group discovered and that led the group to its factual conclusions and recommendations.

Sometimes this practice is helpful to the reader because it alerts the reader to the direction of the report. When the subject matter of the report is as complex as that in this report, this practice does not serve the reader well; because the purpose of a report is to provide the reader with as much background as possible in order that the reader may be able to make an informed judgement upon the recommendations. Such a sneak preview of the ultimate conclusions of the study group may tempt even the most conscientious reader to lose the concentration (in reading the rest of the report) that is necessary for a proper evaluation of those conclusions.

The significance of the central theme of this report can not be overstated. That central theme is the role of the state insurance regulator in seeing that insurance companies will always be able to meet their obligations to the people who buy their insurance policies.

The last time the General Assembly of North Carolina dealt with this subject in any comprehensive manner was in 1971 and 1974, when it enacted respectively the Insurer Holding Registration and Disclosure Act, the Postassessment Insurance Guaranty Association Act (for property and

liability insurance), and the Life and Accident and Health Insurance Guaranty Association Act.

These acts were patterned after model acts that were developed by the National Association of Insurance Commissioners (NAIC), which were in response to a number of serious insurance company insolvencies and some bad experiences in insurance holding company systems that occurred during the nineteen-sixties. The model acts were designed to prevent similar events from occurring after the states enacted them in as similar form as possible, considering any idiosyncrasies within the various states' insurance systems. Even the drafters of these model acts did not believe that the language and spirit of the acts would forever serve the public in the face of changing conditions in the financial and market structures of the insurance industry; and moreover, of the financial services industry, which comprises banking, securities, and insurance.

It is time to act again. The economic dangers, real and perceived, of the nineteen-sixties that led to these model acts as well as the 1974 report to the NAIC by McKinsey and Company, Inc., on the monitoring and regulation by states of insurance company solvency, are once again surfacing. But they are surfacing under different circumstances and in different forms.

Changes in computer science within the last ten years, in federal regulation of banks, savings and loan (thrift) institutions, and securities within the last seven years, and

fairly recent changes in financial services brought about by consumer demands have the real potential of making the task of monitoring insurance company solvency much more difficult for the state insurance regulator.



## COMMITTEE ACTIVITY

Chapter 905 of the 1983 Session Laws (House Bill 1142) authorized the Legislative Research Commission to continue its study of insurance regulation that had been authorized by the 1981 General Assembly. The Commission Cochairmen (Speaker of the House and Senate President Pro Tempore) appointed the members of the Insurance Study Committee and allocated funds in an amount that would allow the Committee to hold five meetings. The Commission was authorized to report to either or both the 1983 General Assembly in June of 1984 or to the 1985 General Assembly upon its convening. Because of time constraints imposed by the General Statutes on the Legislative Research Commission, the study committees of the Commission were required to file their reports with the Commission Cochairmen on or before December 6, 1984. The memberships of the Commission and the Committee appear in the Appendix of this report as Exhibits A and B.

After the members of the Committee were appointed they were periodically provided with information about events in the insurance business, insurance regulation, and integration of financial services. At about the same time, the Conference of Insurance Legislators (COIL), which is a national organization of state legislators who are concerned with insurance regulation, issued a very comprehensive report about deregulation of financial services and the potential effects of that deregulation on the financial stability of insurance companies. COIL issued a supplementary report in

June of 1984, which further defined some of the recommendations in the main report. The COIL Report was furnished to the Committee and influenced the direction of the study toward the important but previously overlooked subject of financial solvency of insurance companies. The Report's transmittal letter from Senator John R. Dunne of New York to Representative Warren D. Arthur, IV, of South Carolina appears in the Appendix of this report as Exhibit C. The introduction and summary of the Report appears in the Appendix of this report as Exhibit D.

The Committee met in Raleigh on September 6, October 3, and November 8 and 29, 1984. At the September 6 meeting John R. Ingram, Commissioner of Insurance, and Robert Hunter, President of the National Insurance Consumer Organization, spoke to the Committee about automobile insurance regulation. Their joint statement appears in the Appendix of this report as Exhibit E.

At the October 3 meeting, presentations were made by Mr. Paul L. Mize, Manager of the North Carolina Rate Bureau and the North Carolina Motor Vehicle Reinsurance Facility; Mr. William Kenneth Hale, Counsel to the Insurance Study Committee; and Mr. James E. Long, who at that time was the Democratic nominee for the Office of Commissioner of Insurance. Mr. Long was subsequently elected to the Office of Commissioner of Insurance in the general election held on November 6, 1984. Mr. Mize spoke, at the request of the Committee, about the origins, structures, and functions of the Bureau

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and the Facility; Mr. Hale summarized and explained the findings and recommendations of the COIL Report; and Mr. Long presented his thoughts and positions on the proper role of the insurance regulator in maintaining the financial integrity of the insurance industry. Mr. Long's statement appears in the Appendix of this report as Exhibit F.

At the November 8 meeting, presentations were made by Mr. Michael S. Olson, on behalf of the Carolinas Association of Professional Insurance Agents, Inc., and by Mr. Hale. Mr. Olson spoke about insurer solvency oversight by the regulator, agents' education requirements, and the role of lending institutions in the marketing of insurance. Mr. Hale explained the provisions of the NAIC model acts for guaranty funds and holding company system regulation. Mr. William Stephenson, Chairman of the North Carolina Industrial Commission, had been scheduled to speak to the Committee about the regulation by his agency of employers who insure themselves, individually or in groups, for liability under the State's Workers' Compensation Act. He was not able to appear because he had to preside at an Industrial Commission hearing. On Mr. Stephenson's behalf, Mr. Hale explained the statutes and regulations concerning those self-insured employers.

Finally, at the November 29 meeting, the Committee reviewed and approved this report.

Minutes (with exhibits) of the meetings of the Committee are on file and available for inspection in the library in the State Legislative Building.



## COMMITTEE FINDINGS AND RECOMMENDATIONS

### FINANCIAL REGULATION OF INSURANCE COMPANIES

#### Forward

There are many aspects of state regulation of the insurance industry. Most purchasers of insurance are aware of the fact that state regulators generally have control over premium rates, policy provisions, and the licensing of insurance companies and agents. One very significant role of the regulator that often goes unnoticed is that of evaluating, regulating, and monitoring the financial conditions of insurance companies that apply for the privilege of doing business in the state and of companies already operating in the state, in order to assure that those companies can fulfill their promises to pay or indemnify their policyholders.

#### Formation and Organization

Insurance regulators must see that the conditions prescribed by their states' insurance statutes for the formation of new companies are enforced. There are initial minimum requirements for paid-in surplus and capital for stock companies and similar minimum surplus and participation requirements for mutual companies. The paid-in capital for a stock company is that dollar value nominally assigned to the company's shares issued to its stockholders. A paid-in surplus is created when, as most states require, the stock is issued so that the value assigned to the stock is less than the money paid in by the stockholders. For mutual companies,

the paid-in surplus funds are usually furnished by lenders, and the participation requirements refer to the number of policyholders insured by the company. The regulator must be able to evaluate these items properly, as well as the characters of the incorporators of the new company. All newly-formed companies are also required to deposit in trust with the regulator securities in a specific amount or in a percentage of the minimum capital or surplus requirements.

### Licensing

Generally, all companies must be licensed by the regulator before they can write insurance in a state. They must furnish the regulator with information about their financial situations to enable the regulator to determine how successful they will be in meeting their policy obligations. Foreign (from other states) and alien (from other countries) companies wishing to be admitted to do business must comply with the same paid-in capital, surplus, and participation requirements as domestic companies that are already operating in the state. All companies by law must maintain in trust with the state a substantial deposit of approved securities; or, in the case of foreign or alien companies, provide a certification from an insurance regulator in another state by which they are licensed that deposits are maintained there to protect the creditors or policyholders of the foreign or alien company.

## Investments

The types of investments that companies may make with their assets are specified in the statutes of most states. Requirements vary among states and between life and health insurers and property and liability insurers. The life and health insurers are usually subjected to stricter investment guidelines because of the long term nature of their obligations to policyholders. The various state laws generally are more restrictive on investments of assets held as unearned premium and loss reserves, but do not require the same investment safety standards for assets such as capital and surplus. Companies are required to file financial statements with the state regulators on annual or more frequent bases. Each statement must list each investment and provide details about the earnings, value, cost, and method of acquisition of each investment. In turn the regulator must determine the values of securities held by the insurance companies in order to judge their financial situations. Fortunately, there is some uniformity in this aspect of regulation: The NAIC has established a securities valuation office, which places values on the securities held in the investment portfolios of about every insurance company in the country. The valuations made by the NAIC are periodically provided to every state regulator as an aid in the financial analyses of the companies regulated.

## Reserves

The methods of computing reserves for property and liability insurers and for life and health insurers are different because of the different natures of their eventual policy obligations. It therefore follows that the reserve requirements for these distinct coverages be different. Property and liability insurers must maintain two types of reserves: One for unearned premiums and one for unpaid losses, both of which are liabilities of the companies. When an insurer collects most or all of the premium at the beginning of a policy term, the portion of the premium collected that, on a pro rata basis, has not paid for the coverage as the policy term elapses is the unearned premium. Once a claim on a policy is known by or has been made against an insurer, the insurer must set aside an amount (in reserve) to pay the claim and related expenses in the event the person making the claim prevails. An insurer must also estimate losses that have been incurred but not known by or reported to the insurer. This must be done to properly determine the insurer's aggregate loss reserve liability for financial accounting and reporting purposes. This is important because loss reserves that are understated can cause insurer insolvencies when claims payments must be made. On the other hand, allowing insurers to place too much in reserves will cause excessive premium rates.

Reserve calculations for a life insurance company are made by computing interest and mortality rates and placing in



ready reserve the amounts that will meet every policy obligation as it becomes payable. For this purpose the NAIC has adopted model standard valuation and nonforfeiture laws, which in turn have been enacted by all of the states.

Health insurance reserve calculations are more complicated, but the purpose is the same as for other coverages. There is an unearned premium reserve; an active-life reserve (where the right of policy cancellation by the insurer is restricted); reserves for claims reported, in course of settlement, approved but not fully paid, incurred but not reported, and claim expenses; and for future contingent benefits.

#### Reporting Requirements and Examinations

Companies are required to file annual (and sometimes quarterly) reports with the insurance regulators of the states in which they write insurance. The report form used by the companies was developed by the NAIC and contains financial information, including premium income, reserves, expenses, and investments. The regulators must verify this information by a direct examination of each company once every three years, which is known as the triennial examination process. In order to minimize confusion and workloads and maximize efficiency among the states, the NAIC has developed a system of four zones in the country. During the examination the insurance regulators from the insurer's domiciliary state presides, and no more than one examiner from each of the other three zones participates. Each state

in which the insurer does business is therefore represented in the process by an examiner from its zone. The cost of the examination is paid for in full by the company being examined.

### Analysis of Financial Statements

During the three-year period between company examinations an insurance regulator must rely on the annual financial statements for information that would indicate a trend toward insolvency for any insurance company. With the exception of a few states, regulators examine the financial statements manually, without the benefit of electronic data processing. With the breakthroughs in data processing that have occurred and that are being utilized fully by insurance companies, regulators without access to computer technology are at a disadvantage. The most important factor in solvency analysis is the adequacy of a company's loss reserves. With computers, the companies are able to quickly analyze their reserves, as well as their liquidity, which is just as important on the asset side of their ledger books. Companies transfer funds electronically, but these transfers are known to the regulator only once a year and well after the fact.

The information required to be on the annual financial statements is compiled by the companies at the end of each calendar year and sent anywhere from two to three months later to the regulator. At that point the information is already somewhat dated. The regulator conducts "desk audits"



of the statements and, after ascertaining the accuracy of the information on the statements, compares the year-end results of those statements with those of prior statements.

The NAIC has developed the Insurance Regulatory Information System, known as the "early warning system," to help the state regulators analyze this data. The NAIC receives annual statements from the regulators shortly after March 1 of each year, and puts the data into computer-readable format. The computer then analyzes the data by the application of the following test ratios for solvency: Premium to surplus, change in writings, surplus aid, two-year operating, investment yield, change in surplus, liabilities to liquid assets, agent balance to surplus, one-year and two-year reserve development, and current reserve deficiency. Examining teams then study the statements of those companies whose data produce four or more ratios that stray from the norm. The NAIC sends the preliminary results back to the regulators, and subsequently forwards the conclusions and recommendations of the examining teams' studies. On paper this is a great system, but in this time of instantaneous electronic transfers of assets and liabilities, the fact that most of the insurers' financial statements and the NAIC's early warning system are on annual bases requires a rethinking of the states' reporting requirements for insurers. By the time a company's financial situation is fully understood, it could very well be too late to take corrective regulatory action. This means that even on-line

access by regulators to the early warning system would fall short of what is needed.

#### RECOMMENDATION

The North Carolina Department of Insurance should be provided with the electronic data processing equipment and additional in-house examiners and other personnel that will enable the Department to instantaneously verify the accuracy of financial statements, run test ratios on the data in the statements similar to those in the NAIC early warning system, and make analyses of trends and projections based on the data. The early warning system's present capabilities do not allow such trend analyses or projections, but only allow test ratio analyses to the results of prior years.

Once the Department is automated, the companies should be required to prepare and file quarterly financial statements. All of this would greatly reduce the delay from the occurrences of company financial activities to the preparations of the statements and from the filings of the statements to the proper analyses of the financial data contained in the statements.

The NAIC is presently working on a system whereby key financial data could be fed into a central computer, coordinated by the NAIC, and transmitted to all states on a timely basis. The data could then be fed at each regulatory agency into a microcomputer using commercially available software.

The exact cost of acquiring and installing the necessary equipment and the exact number of personnel (computer operators/programmers and financial examiners) required for this needed step are not known as of the date of this report. However, by the time the appropriations process gets under way during the first regular session of the 1985 General Assembly, the Commissioner of Insurance will have this information for the members of the General Assembly.



## INSURANCE HOLDING COMPANY SYSTEMS

### Background

During the business conglomerate buy-ups, bidding wars, and other intense corporate activity during the early and middle nineteen-sixties, it became obvious to insurance regulators that insurance companies were prime acquisition targets. The companies themselves were aware of this and in turn were interested in attracting more capital for growth and in diversifying their business interests. Stock companies were interested in "upstream" non-insurance corporations to hold their stock; and mutual companies were looking for "downstream" subsidiaries. The NAIC recognized a real danger for regulators trying to monitor these corporate developments. The potential harm to insurance policyholders was great if, for example, a predatory parent company transferred assets of a subsidiary insurer so as to render the insurer financially unable to meet its policy obligations; or in the same vein, if a stock insurer was acquired by another company through sale of a controlling interest of its stock to that company, and the insurer declared a huge stock dividend in order to benefit the parent company, thus impairing the insurer's assets.

The first legislative response to these corporate mergers was passage by Congress of the Williams Act to protect shareholders from any lack of neutrality between the acquiring and target corporate managements; and to guarantee that all investors had the same information in order to decide whether to buy or to sell. The second legislative response was the

enactment by many states of business takeover statutes, which required registration with state regulators before any takeover offer could begin, in order to protect investors within the respective states. The U.S. Supreme Court in Edgar v. Mite Corp., 457 U.S. 624, 102 S.Ct. 2629, 73 L. Ed. 2d 269 (1982), declared the Illinois version of the business takeover act unconstitutional because it was an excessive burden on interstate commerce and was preempted by the Williams Act. The third legislative response was adoption by the NAIC in 1969 and subsequent enactment by many states of the Insurance Holding Company Systems Regulatory Act.

#### The NAIC Model Act

The purpose of the act is to provide state regulators with the information about insurance holding company systems that will enable them to monitor the financial status and fiduciary standards of the insurers they regulate. The act provides for registration and the filing of pertinent information, such as who controls the insurance company through stock ownership and what transactions or other activities are conducted by the insurance company with its affiliates in the system. Transactions with affiliates must be fair and reasonable and may not impair the surplus of the insurer with respect to its policyholders. The stock dividends declared by the insurer for its shareholders are subject to close regulation; and any dividends out of the ordinary must be reviewed by the regulator prior to any payment to shareholders.

Any changes in corporate control of domestic insurers are subject to approval by the regulator, who must determine whether or not the change will assure a continuation of the stable operation and financial soundness of the domestic insurer and will be in the best interest of the company's policyholders. Information about proposed changes that must be provided to and reviewed by the regulator include financial, operational, and biographical information about the company wishing to acquire the domestic insurer, as well as proposed plans for the insurer that reflect upon the management philosophy of the would-be acquiror.

#### Significance Today

The insurance holding company systems registration and disclosure legislation in effect in a state is becoming increasingly important to the insurance regulator in light of recent developments in financial services -- integration of financial institutions' corporate structures, the introduction of new products (for example, cash management accounts, money market funds, automated teller machines, credit card operations, and combination life insurance/investment vehicles), the mixed, partial deregulation of banking and securities by the Comptroller General, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Securities and Exchange Commission, and efforts by members of Congress to legislate the deregulation of banks and thrift institutions. These developments have been and will be brought about by consumer demands, forces in the economic



marketplace, and the desire of each segment of the financial services industry to diversify its product line and penetrate new markets in and to which it can sell its products.

#### RECOMMENDATION

As evidenced in Edgar v. Mite, the U.S. Supreme Court is not reluctant to nullify state laws affecting interstate commerce if it finds them to be burdensome, nor is it reluctant to hold that federal law controls if there is a federal statute or regulation governing the same subject. Shortly after Edgar v. Mite the NAIC reviewed the model act and made revisions thought to be necessary to make the act comport with the decision of the Court. The NAIC is presently conducting a comprehensive review of the model act and hopes to present its recommended revisions for adoption at the NAIC Winter Annual Meeting, which will take place December 9-14, 1984.

One of the recommendations of the COIL Report, and endorsed by the NAIC, was that all states should have insurance holding company systems regulatory acts patterned after the NAIC model. Uniformity of state regulation will lessen the chance of another federal court ruling that declares the state law must fall because it creates an impermissible burden on interstate commerce, and will lessen the chance of Congressional action that would preempt state laws in this area.

The North Carolina General Assembly enacted Article 12A of General Statutes Chapter 58 (G.S. 58-124.1 through 58-124.11) in 1971. Article 12A was patterned after the 1969



NAIC model act, but no legislation has been introduced in the General Assembly to incorporate the subsequent NAIC model act revisions into North Carolina's law. The 1985 General Assembly's House and Senate Insurance Committees should examine the NAIC revisions to the NAIC Insurance Holding Company Systems Regulatory Model Act and consider amending North Carolina's law to reflect those revisions. If the NAIC does not reach a consensus on the most recent revisions in time for 1985 legislation, the 1985 General Assembly should at least consider updating the North Carolina law to reflect the present state of the NAIC model act.



## INSURANCE GUARANTY FUNDS

### Background

An insurance guaranty fund is simply an arrangement for pooling the funds of solvent insurance companies in order to pay certain claims against, or continue the coverage that had been provided by, an insolvent insurer. The guaranty fund concept did not begin with the adoption by the NAIC of model acts for property and liability insurance in 1969 and for life and health insurance in 1971. A number of states, including North Carolina, enacted security funds in the nineteen-thirties to cover claims in workers' compensation insurance. New York enacted the first life insurance guaranty fund law in 1941. But a rash of insurance company insolvencies in the early nineteen-sixties, particularly in the substandard automobile insurance market, left many accident victims without any compensation and resulted in a serious proposal in Congress for a federal guaranty system for insurance similar to that for banks and thrift institutions. That threat of federal regulations led to the NAIC model acts and subsequent enactment of those models by a majority of the states for life and health insurance and by all of the states for property and liability insurance.

Unfortunately, there are too many variations in these laws among the states; and as recognized in the COIL Report and by the NAIC, this lack of uniformity could lead to a renewed interest in a federal guaranty system. Such action by Congress would not be unprecedented, for Congress has

taken steps in flood, crop, urban and coastal property, and Medicare supplement insurance coverages whenever it became apparent that there was either a lack of uniformity among the states or an unwillingness on the part of the states to act.

#### The NAIC Model Acts

The NAIC acts are similar in form and operation, but differ in the following respect: While the purpose of the property and liability fund is to pay insurance claims, refund unearned premiums of an insolvent company, and provide continued coverage for up to thirty days after the company has been declared insolvent, the life and health fund goes further by continuing coverage for the insolvent company's policyholders. Also, the property and liability fund is not triggered until there is a judicial determination of insolvency; whereas the life and health fund is triggered upon a finding by the regulator that a member company is impaired, in which case the fund may guarantee, assume, or reinsure the policies of the impaired insurer, or see that it is done, and assess the members for the cost of doing so.

Both model acts are similar in that they provide for the creation of a nonprofit association with a governing board to administer the fund; mandatory membership and participation in the fund by all insurers licensed to write the particular coverages in the state; a dollar limit on individual claims and coverages; coordination and cooperation between the insurance regulator and the board of governors when the fund has been activated by a member insurer's insolvency; a line

of communication between the regulator and the board to detect and prevent insolvencies; approval by the regulator of the plan of operation of the fund; and assessments of member companies in the form of a percentage (four percent for life and health and two percent for property and liability) of each member's net direct written premiums for the preceding calendar year.

#### North Carolina Legislation

The North Carolina General Assembly enacted guaranty fund laws for property and liability insurance in 1971 (Article 17B of General Statutes Chapter 58, G.S. 58-155.41 through 58-155.60) and for life and health insurance in 1974 (Article 17C of General Statutes Chapter 58, G.S. 58-155.65 through 58-155.84). With some exceptions in the 1974 legislation, both acts were patterned after the NAIC model acts that were in existence then; however, the NAIC has made some revisions in the model acts since their dates of adoption, most of which have not been even introduced in the North Carolina General Assembly.

#### RECOMMENDATION

The NAIC is now in the process of revising both model acts. Some of the items being examined are extraterritorial liability for insolvent domestic insurers, "no frills" continuation policies that are actuarially sound, policy liability limits, triggering mechanisms, and pre-funding instead of post-insolvency assessments. The NAIC hopes to

have the revisions to the life and health model act ready for adoption at the NAIC Winter Annual Meeting, and the revisions to the property and liability model act ready for adoption by early June of 1985.

For the same reasons the COIL Report recommended uniformity among the states in enacting the provisions of the NAIC's model act on insurance holding company systems regulation, it also recommended uniformity among the states in enacting the NAIC's model acts on insurance guaranty funds. It could be said that because of the aforementioned federal interest in this area in the middle nineteen-sixties, and because of the awareness of many people now of the consequences of a huge insurer insolvency, it behooves the states to attain uniformity by making their laws comport with the NAIC model acts. This has been successfully done by the states in other areas of law, particularly in commercial transactions, of which the Uniform Commercial Code is a good example.

The 1985 General Assembly should, through the House and Senate Insurance Committees, examine North Carolina's guaranty fund laws and, assuming the NAIC adopts the revisions presently under consideration, evaluate those revisions with an eye towards improving North Carolina's law and achieving the uniformity so badly needed among the states. If it appears that the revisions will not be adopted in time for 1985 legislation, the General Assembly should at least update

its guaranty fund laws to reflect the present states of the  
NAIC model acts.





## WORKERS' COMPENSATION

### Self-Insurance

Under the North Carolina Workers' Compensation Act, the employers covered by the Act are required to either purchase workers' compensation insurance from a licensed insurer or provide the North Carolina Industrial Commission with proof of the ability, either alone or in a pooling arrangement, to pay compensation to employees as prescribed in the Act. N.C. General Statute §97-93 further authorizes the Industrial Commission to require those employers who are self-insured to deposit with the Commission securities, indemnities, or bonds with the Commission, along with evidence of reinsurance, that are sufficient to guarantee payment of workers' compensation claims.

Rule V of the Industrial Commission sets out the financial and actuarial prerequisites for qualification as a self-insurer, and the security deposit, reinsurance, and indemnity agreement requirements for self-insurers. In reviewing applications made by employers who want to be self-insured, the Commission must analyze the assets, liabilities, claims experience, and risk factors of each applicant in the same manner that the insurance regulator would review the application of a company that wants to underwrite workers' compensation insurance in the State. Furthermore, the Commission must continuously review the financial conditions of self-insured employers in the same manner that the insurance regulator would monitor the

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solvency of an underwriter of workers' compensation insurance. Rule V appears in the Appendix of this report as Exhibit G.

#### Security Fund

Since 1935, North Carolina has had a mechanism for covering workers' compensation claims that would go unpaid because of the insolvency of the insurance company obligated to pay the claims on behalf of an employer. Article 3 of General Statutes Chapter 97 (G.S. 97-105 through 97-122) created separate security funds for stock and mutual companies and reciprocal or interinsurance exchanges that are authorized to underwrite workers' compensation insurance in North Carolina. Unlike the guaranty associations for life and health and property and liability coverages, which assess the member companies after one of the companies becomes insolvent, these accounts are funded by the member companies and are maintained by the State Treasurer. The Commissioner of Insurance administers these funds, and is authorized to review applications for payments from the funds and provide for payments from the funds by certification to the State Treasurer.

#### RECOMMENDATION

Regulation of companies that underwrite workers' compensation insurance and employers who prefer to insure themselves against workers' compensation claims by their employees should be the responsibility of one State agency, not

two. The Department of Insurance should assume the function of approving and regulating self-insured employers. Such consolidation of workers' compensation insurance regulation would be more cost-efficient for the State because of the similarities of the factors that must be analyzed for approval to underwrite or self-insure and for solvency protection. In order to avoid the necessity of additional appropriations to the Department of Insurance for this purpose, appropriate adjustments should be made in the budgets of the Departments of Commerce and Insurance to allow for the transfer of this role. In addition, any necessary personnel transfers from the Industrial Commission to the Department of Insurance should be made. Legislation to effectuate this recommendation appears in the Appendix of this report as Exhibit H.



## INSURANCE STATUTES REWRITE

Since 1899, when the General Assembly created the Office of Insurance Commissioner and the Department of Insurance, almost every General Assembly has enacted laws to provide for the regulation of insurance. These enactments have ranged from brand new provisions, some of which were patterned after model acts, to patchwork amendments that were in response to conditions prevailing before the times of enactment.

With the possible exception of the North Carolina Commission on Revision of the Insurance Laws, which issued a report in 1945, there has never been a comprehensive review of North Carolina's insurance statutes. This is not to say that the General Assembly has not undertaken the task of analyzing the role of the State in regulating insurance on a grand scale. The 1977 revisions in property and liability insurance rate regulation indicate that there has been such an effort. There just has not been enough time and resources for the General Assembly to conduct such a review. It would be difficult at best for the General Assembly's standing insurance committees to develop broad changes in or voluminous recodifications of the insurance statutes during any legislative session; and since 1975, the four legislative Research Commission studies on insurance have had to work with very limited budgets and therefore very limited resources.

Considering the time and fiscal constraints under which these standing and study committees have labored and the relative progress that they have made, it would seem that an all out effort to rewrite and rearrange North Carolina's insurance statutes could result in a statutory framework that is readable, internally consistent, unambiguous, and responsive to the needs of the public.

The Supreme Court of North Carolina has at more than one time expressed its dismay at the state of our statutes. In State ex rel. Commissioner of Insurance v. North Carolina Fire Insurance Rating Bureau, 292 N.C. 471, 234 S.E.2d 720 (1977), the Court stated:

We observe that both the Commissioner and the Bureau are enmeshed in a statutory plan for rate-making so ambiguous and unclear that legislative revision appears to offer more likelihood of future harmony between the Commissioner and the Bureau, in their effort to bring about a realization of the dual legislative purpose of insurance at a reasonable cost in financially responsible companies, than does piecemeal construction of the statutes through what is not rapidly assuming the proportions of an interminable series of judicial reviews of orders by the Commissioner.

Three years later, in State ex rel. Commissioner of Insurance v. North Carolina Rate Bureau, 300 N.C. 381, 269 S.E.2d 547 (1980), the Court said:

The North Carolina General Assembly has effectively and properly delegated insurance ratemaking to the Rate Bureau with review by the Commissioner of Insurance. It can, and perhaps should, review the statutes with the view to providing clarity on such significant substantive matters as that presented here. In the meantime, it is incumbent on the Commissioner, in discharging the broad powers he possesses as head of a major State administrative agency, to follow the clear lawful procedures prescribed by our Legislature to guide all administrative agencies.

In State ex rel. Hunt v. North Carolina Reinsurance Facility, 302 N.C. 274, 275 S.E.2d 399 (1981), the Court, after recounting its statement in the 1977 case, delivered another message to the General Assembly and to the Commissioner of Insurance:

Unfortunately, this piecemeal construction of our insurance statutes has continued. Indeed, during the past eight years, the appellate division has issued over thirty opinions resulting from actions before the Commissioner of Insurance. Although



resolving such disputes is, of course, the proper function of the appellate courts, we do not think it unreasonable to observe that these disputes are far too numerous and that the legislative intent behind our insurance statutes should not be so difficult to discern that almost quarterly decisions from the judicial branch of government are required. We think the Legislature should hasten to rewrite the insurance laws in question in clear and unmistakable language.

\* \* \*

Our Legislature, therefore, is presented with no enviable task. It must, as our statutory architect, evolve a plan which will best protect the public interest and ensure the liquidity and solvency of participating insurance companies in our state who must also be assured of a reasonable profit. This balancing of equities between the consuming public and the commercial sector can be done only by the legislative branch and the plan can be effectively administered only with the full cooperation of the executive branch of government. Most importantly, the Legislature, in formulating a regulatory scheme, should employ words that clearly and

accurately reflect its intent so that the courts of this state will have some much needed guidance in interpreting those laws.

#### RECOMMENDATION

It is incumbent upon the 1985 General Assembly to authorize a study of the insurance statutes with the view toward the goals mentioned by the Court. Only a well-funded study can accomplish this task. The group should be able to meet monthly and, if necessary, hire professional or clerical staff from outside of the General Assembly and Department of Insurance.

Because of the traditional differentiation in the regulation of property and liability insurance on the one hand and life and health insurance on the other, those two areas should be separately studied. The Commission should undertake the property and liability segment first, because that area has been the main source of the problems mentioned by the Court. The Commission should begin its study immediately after the adjournment of the first regular session of the 1985 General Assembly, be authorized to make an interim report to the 1986 regular session of the 1985 General Assembly, and make a final report to the 1987 General Assembly.

After the first regular session of the 1987 General Assembly adjourns, the Commission should begin its study of the life and health insurance statutes; however, the Commission should be given the flexibility to continue any

unfinished business in the property and liability insurance statutes and report its findings and recommendations along with those pertaining to the life and health insurance statutes. In any event, the Commission could submit an interim report to the 1988 regular session of the 1987 General Assembly and a final report to the 1989 General Assembly.

The Commission should consist of twelve persons, four appointed each by the Speaker of the House, the Lieutenant Governor, and the Commissioner of Insurance. The Commission to study property and liability insurance statutes should consist of two public members, two property and casualty insurance agents, two property and casualty insurance company representatives, three House members, and three Senate members. The public members and legislators should not have any direct, substantial financial interest in any insurance company.

The composition of the life and health study group will have to be somewhat different in recognition of the different market structure of that industry. But that should be left to the 1987 General Assembly. The proposed legislation, which appears in the Appendix of this report as Exhibit 1, establishes only the property and liability insurance study group.

## CONCLUSION

This study has been only the beginning of the State of North Carolina's effort to improve its protection of people from the dangers of financial instability in insurance markets. The 1985 General Assembly has an opportunity to make this improvement first by assuring that the North Carolina Department of Insurance has the personnel and equipment that are required to monitor insurance company solvency in these new times of complicated financial transactions and intricate business structures; and second by shoring up state laws that require financial integrity of insurance companies and state laws that address situations of insolvent insurers and their policyholders. This report has been designed to serve as an aid to the members of the 1985 General Assembly (and future Assemblies as well) when the time comes to make decisions on these matters.



STATE OF NORTH CAROLINA  
LEGISLATIVE RESEARCH COMMISSION  
STATE LEGISLATIVE BUILDING  
RALEIGH 27611



LEGISLATIVE RESEARCH COMMISSION  
1983-84

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STATE OF NORTH CAROLINA  
LEGISLATIVE RESEARCH COMMISSION  
STATE LEGISLATIVE BUILDING  
RALEIGH 27611



INSURANCE STUDY COMMITTEE  
1983-84

LRC Member Responsible for Study

Representative Margaret Tennille  
Winston-Salem

Committee Cochairmen:

Representative Foyle Hightower, Jr.  
Wadesboro

Senator Joseph E. Johnson  
Raleigh

Committee Members:

Representative Frank W. Ballance, Jr.  
Warrenton

Representative Charles M. Beall  
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Senator J. J. Harrington  
Lewiston

Representative John Calvin Hasty  
Maxton

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Lenoir

Representative Hugh A. Lee  
Rockingham

Representative Mary P. Seymour  
Greensboro





JOHN R. DUNNE  
6<sup>TH</sup> DISTRICT

THE SENATE  
STATE OF NEW YORK  
ALBANY

Exhibit C

September 14, 1983

Representative Warren D. Arthur, IV  
President, Conference of Insurance Legislators  
House of Representatives  
Columbia, South Carolina 29211

Dear Warren:

It is a pleasure to submit to you this report of the COIL Task Force on Regulatory Initiative which was created by resolution at COIL's 14th Annual Meeting in New York City in November 1982. The resolution provided:

RESOLVED the Conference of Insurance Legislators establish an ongoing task force to make findings concerning the ability of state insurance departments to respond to issues and problems evolving in insurance; and be it

FURTHER RESOLVED, that the first subject of the task force study be the development of the financial supermarket and multi-purpose financial products.

In carrying out our first charge, the Task Force has attempted to determine how regulators can allow free enterprisers to fulfill their desire to ally themselves with new partners without compromising the basic public policy goals of insurance regulation. We specifically have not addressed the substantive question of whether insurance and other financial service businesses should integrate.

We have examined recent mergers, holding company and conglomerate formation, and integrated financial service product development in light of the longstanding goals of insurance regulation, namely, to see that people get their money's worth, that they can deal with solvent insurers that sell in strong, adequate, and competitive markets, and that insurers treat people fairly.

With those goals in mind, we have also examined

- the performance of conglomerates and holding companies to determine how in some cases the holding company device has served or failed to serve the public interest;
- the risks involved in the affiliation with insurers of banks and securities houses;
- the impact and opportunities deregulation of financial services poses for insurance brokers and agents; and

## Exhibit C

-- how financial services industries have moved far ahead of regulators in their use of state-of-the-art computer and telecommunications systems.

Our studies lead to the conclusion that with the benefits promised by deregulation there are some real dangers. Even though state insurance departments have in the past carried out their statutory responsibilities in a highly commendable way, they do not have the equipment or personnel resources to adequately regulate -- in this day of complex financial products -- holding company pyramids and instant telecommunications and fund transfers.

Our response has not been to cry halt to deregulation, but instead to propose "re-regulation," an improvement and extension of the regulatory function to monitor for solvency so that, when necessary, regulators can promptly move in to halt actions which endanger the financial health of insurers.

If deregulation and the crossbreeding of financial institutions and instruments are to continue in ways that afford maximum safety for insurance buyers, legislators will have to provide insurance departments with the means to do their job. That includes the equipment and resources that will help them monitor the industry and, thereby, spot any serious danger to insurer solvency at a very early date.

Legislators need to reinforce and strengthen laws that provide for the walling-off of insurance company reserves, surplus, and assets from other enterprises with which they are affiliated. And in view of the concentration of risks involved in the merger of financial institutions, legislators should take added steps to make certain that insurance guaranty fund laws are broadened to provide for maximum protection of insurance policyholders in the event of an insurer insolvency.

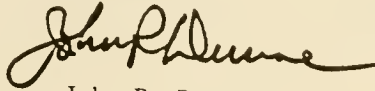
Our inquiries have convinced us that greater legislative participation in the regulation process is absolutely necessary. We have also concluded that state legislators must communicate directly with the members of Congress to assure that state regulatory problems, as well as achievements, are understood and that different financial service institutions serve their customers in a manner which serves the public interest.

The Task Force and its professional staff have conducted extensive research and analyses. It received testimony from witnesses at a public hearing in New York City on March 20, 1983; examined hundreds of both primary and secondary source documents; and conducted more than one hundred interviews. The Task Force held meetings on February 12, March 18, April 30, August 12 and September 14, 1983. This entire undertaking would not have been possible without the extraordinary personal commitment of the staff director, Robert Mackin, and Peter Strauss, who directed the research effort. Only their untiring dedication to our mission made this report a reality.

Exhibit C

The members of the Task Force, the staff and I are extremely grateful to you for providing us with the opportunity to perform this very important charge. Your leadership in the coming months will be the impetus with which members of COIL can lead the efforts to bring about the changes these times demand.

Sincerely,

A handwritten signature in dark ink, appearing to read "John R. Dunne". The signature is fluid and cursive, with the first name "John" being more prominent and the last name "Dunne" following in a similar style.

John R. Dunne



Although the integration of financial services may well promote competition, it is imperative that this phenomenon be properly regulated.

Exhibit D

James P. Corcoran

NYS Superintendent of Insurance

June 1983

## INTRODUCTION AND SUMMARY

In the fast mix and match of their companies and products, America's financial leaders<sup>\*</sup> are doing some imaginative things with other people's money. Many of their efforts are very worthwhile. But others are proving a little too inventive, aggressive, and perhaps even reckless, and have raised serious questions as to the ability of regulators to keep watch.<sup>1</sup>

The situation points clearly to a need to reaffirm fundamental regulatory goals and give government agencies what they do not have now -- the human and technical resources to meet those goals.<sup>2</sup> At the same time, it demands the resolve to encourage development of strong financial institutions free to innovate and offer competitive products and prices, while keeping their covenant of good faith with the consumers of their services.

This report views events and makes recommendations from the perspective of state legislators concerned with insurance regulation, and analyzes issues and problems in the context of the economic and political realities which have helped shape them. And it is those realities which public policy makers must face if they are to succeed in resolving those issues.

The events addressed in this report are taking place at great speed. Almost overnight and coincident with the high degree of public acceptance of "deregulation," the giants of banking, securities, insurance and other financial

services have brought together their separate, sometimes rivalrous, enterprises to form conglomerates and holding companies.<sup>3</sup> They have begun to covet and reach out for each other's customers, cash flow and market shares. They have also begun to use selling methods and to offer products that are innovative and useful, but quite different from what buyers and regulators have ever seen.<sup>4</sup> Already, unfamiliar structures and products have proven very risky for the investor<sup>5</sup> and difficult for the regulator to control.<sup>6</sup> It is far from certain who will fare best.

For months, a piano maker-turned-financial conglomerate has teetered on the brink of insolvency with some market experts questioning the ability of its insurance subsidiaries to meet their obligations to policyholders.<sup>7</sup> Though much remains for authorities to learn about the episode, it is reasonable to say now that, judged by traditional insurance industry standards, it sold too much, too fast and, in doing so, blew the fuses out of existing regulatory monitoring systems.<sup>8</sup> It is an episode which shows the need to strengthen insurance holding company and guaranty fund laws.

The state regulatory apparatus is underfunded, understaffed, and underequipped.<sup>9</sup> That should come as no surprise. Though Americans and their legislators have been most generous in assigning large and important tasks to government regulatory agencies, they have been consistently stingy in providing them with the resources to do the job, let alone address fundamental issues or prepare for major challenges.<sup>10</sup>

No one need look to know where the blame lies. Governors, insurance commissioners, and legislators all must share responsibility for the present situation where, even in this day when the computer is commonplace especially in the financial services industry, regulators work mainly with manual systems and outdated calculators.<sup>11</sup>

When it comes to computers, while the state-of-the-art is futurist, the art of the states is an heirloom.<sup>12</sup> The much touted "early warning system" of the National



Association of Insurance Commissioners (NAIC)<sup>13</sup>, for example, as it now operates, may not spot and relay information of potential insurer impairment or insolvency until months after the danger should have become clear.<sup>14</sup> With the increase in holding company formation, which makes things more complex, and the ever changing product lines and tax structures, state insurance department and NAIC procedures that monitor for insurer financial condition are too slow.<sup>15</sup>

But watchdogging for solvency will take more than funding and technical updating. Once formidable barriers, that had their beginnings in the first hundred days of the New Deal, to keep banks, insurers and securities houses separate -- and to strengthen the competitive tensions between them<sup>16</sup> -- are now hardly more than Maginot Lines which aggressive managements can easily outflank.<sup>17</sup> Most recently, state governments, eager to add new financial service corporations to their economic base, have welcomed lobbying efforts aimed at gaining access to insurance markets and cash flow.<sup>18</sup> That states are willing to go so far to win more business is a consistent fact of life in today's real world of fiscal and economic uncertainty.

At the national level, Congress, with input from the states, should act decisively to formulate a national policy as to whether banks, insurance companies, and other financial services should get into each other's business and, if so, with what safeguards for solvency. That subject was outside the charge of the Task Force. But state and national leaders should give immediate attention to its thorough study and resolution.

Any consideration of the regulatory issues involved in merged financial institutions must take into account the present disarray and fragmentation of existing agencies at both the state and federal levels.<sup>19</sup> It appears at first thought to beg for consolidation and reordering and, perhaps, for the creation of super-federal and super-state bodies which would mirror the realities of financial services operations. But there is little prospect that schemes for such



consolidation will be especially productive.<sup>20</sup> They are easy to put on paper, but are likely to prove impractical when tested in the legislative process where politics and bureaucratic self-interest would harden natural resistance to change.<sup>21</sup>

Instead, a far more practical alternative is re-regulation -- the strengthening of existing safeguards for solvency and the streamlining of the state insurance departments' watchdog function. That will encourage innovation and efficiency and keep state regulators on the playing field, level or otherwise, and help them to see what's going on -- as it happens, and in time to achieve their primary mission, the preservation of solvency.

## INTRODUCTION FOOTNOTES

\*

For the body of this report, unless specifically mentioned, the following terms will be used with the following meanings:

Banks	-- includes all commercial banks, savings mutuals, savings and loan associations and credit unions.
Insurance Company or Insurer	-- includes property/casualty firms and life/health firms but does not include "Doctors' mutuals," Blue Cross or Blue Shield.
Security House/Security Firm Brokerage House/Brokerage Firm	-- investment bankers dealing in stocks, bonds and debentures whether over-the-counter or on a registered exchange.
Insurance Producer	-- insurance agent, insurance broker, agency or insurance brokerage firm.

Further, the term "financial services industry" is used extensively. The American Council of Life Insurance, in its December, 1982, report, "Financial Services in the 1980's" (p.6) said:

In its broadest sense, the term encompasses all organizations or parts of organizations that are engaged in financial transactions or in the provision of services related to financial transactions. For analytical purposes, however, it is sometimes more helpful to look to the collection of firms or divisions of firms that are active principally in the business of lending money, managing money, making markets, transferring funds, or providing insurance.

The Hudson Institute noted (in an unpublished paper, dated December, 1981), that this latter type of definition includes commercial banks; savings and loan associations; mutual savings banks; credit unions; investment bankers; mortgage bankers; broker-dealers; mutual funds; pension funds and pension fund managers; insurance companies; finance companies; factoring and leasing companies; stock, commodity, currency and insurance exchanges; corporate treasurer's offices; and government lending and insurance agencies.

1

Rors, Nancy L., "Bank Regulators Panting to Catch Up," **Washington Post**, April 6, 1983, p. A1; Letter dated December 31, 1982, from William H. L. Woodyard III, Arkansas Insurance Commissioner, to all insurance commissioners regarding Arkansas Department examination of Baldwin-United Corporation affiliates domiciled in Arkansas, pp. 5-6 (hereinafter, Woodyard Letter). See also: Request for Comments of the Office of the Vice President, Federal Regulation of Financial Services, **Federal Register**, February 7, 1983, pp. 5704-5707; "Homogenization of Financial Institutions: The Legislative and Regulatory Response," **The Business Lawyer**, November, 1982, pp. 241-270; **Hearings before the Senate Committee on Banking, Housing and Urban Affairs on the Condition and Structure of, and Competition Within, the Domestic Financial Services Industry**, 98th Congress, 1st Session (1983), April 26 and 27, 1983, (statements of Donald T. Regan, C. Todd Conover, William M. Isaac and Richard T. Pratt), (hereinafter, U.S. Senate Hearings on the

Financial Service Industry); **Proceedings of the Eighty-Second Annual Meeting of the Conference of State Bank Supervisors**, (May, 1983), (comments of Congressman Jerry M. Patterson, Congressman Bill McCollum, William C. Harris and Richard M. Dominguez), (hereinafter **CSBS Proceedings, 1983**); "The Changing Environment for Financial Services and Products," **The Business Lawyer**, February, 1983, pp. 667-706.

2

As experienced by the Arkansas Insurance Department in its examinations of the National Investors Life Insurance Company and the National Investors Pension Insurance Company of December, 1981, and September, 1982, note 7, *infra*; **Hearings on S.1710 Before the Senate Committee on Banking, Housing and Urban Affairs**, 95th Congress, 1st Session (1977), September 12, 13 and 14, 1977, (Statements of Harold M. Williams, James M. Stone, Keith R. Rodney and Jean C. Hiestand), (hereinafter, **U.S. Senate Hearings on S.1710 (1977)**); McAlear, Charles, "Insurers Can Go Down the Drain," **Business Insurance**, June 13, 1983, pp. 23-24; **Hearings Before the Conference of Insurance Legislators Task Force on Multi-Purpose Financial Products and Regulatory Initiative**, (March 18, 1983), (statement of William H.L. Woodyard III), (hereinafter **COIL Hearing**); **Report of the National Association of Insurance Commissioners Special Joint Committee on Examinations (Exposure Draft)**, February, 1982, (hereinafter **NAIC Bell-Budd Report**). See also **Alliance of American Insurers, NAIC In Transition**, (1982), pp. 43-48 and pp. 57-59; **1982-1983 National Association of States' Information Systems Annual Report**.

3

For example: the merger of Connecticut General Corporation and INA Corporation, two of the largest insurers in the United States, to form CIGNA; the purchase of Bache, Halsey, Stuart by Prudential Insurance Company in 1981 and the subsequent purchase of Capital City Bank of Hapeville, Georgia, in 1983; the acquisition of the Crum and Forster Group by the Xerox Corporation in 1983; the acquisition by BankAmerica of Charles Schwab Corporation, the largest discount brokerage chain in the country; the partnership of Aetna and Midland Bank of Britain and Aetna's ownership of Federated Investors, the nation's leading mutual fund management firm; the acquisition by E.F. Hutton of The Life Insurance Company of California, later renamed E.F. Hutton Life.

4

The Dreyfus Consumer Bank, formerly the Lincoln State Bank of East Orange, New Jersey, has divested itself of the commercial loan aspect of its business. Thus, it is not by definition a "bank" (12 U.S.C. § 1841). The bank has embarked on an aggressive marketing program to attract noncommercial business. It is undercutting most home mortgage and auto financing plans and is offering other new products to the banking world such as borrowing against equity values in homes and money market funds. McMurray, Scott, "Dreyfus Renames New Jersey Bank," **American Banker**, April 13, 1983, p.3.

E.F. Hutton Life was the first to offer a universal life insurance policy and based on its success, they have almost completely cut out their other business (Task Force Staff Interview with Janet Muncie of E.F. Hutton Life). The policy is a combination death-risk coverage plan and a high yield investment which permits policyholders to adjust their premiums on a yearly basis to suit their needs (Miller, Lynn C., and Richard M. Williams, "Universal Life: The Product of the Future?" **Best's Review** (Life Edition), September, 1981, p. 32). The return on the investment portion on many firms' universal life policies has been as high as 14 percent (Reardon, Michael, "Universal Life Comes to Unionmutual," **Impact**, December, 1981).

Security Pacific National Bank was the first bank to offer securities brokerage services to its customers; over 600 banks have followed suit. In 1982, BankAmerica purchased Charles Schwab Corporation, bringing together the largest

commercial bank and the largest discount brokerage. Hector, Gary, "The Banks Invade Wall Street," **Fortune**, February 7, 1983, pp. 44-48.

In 1979, Baldwin-United Corporation persuaded 65 security houses to sell a relatively unknown insurance/investment product through their national sales forces. The commissions on the sales of Baldwin's insurance affiliates' single premium deferred annuities (SPDAs) were high for the brokerages, and their customers found the product's tax advantages and investment aspects very attractive. Woodyard Letter, *supra* note 1, at 1.

Cash management services, first offered by Merrill Lynch, combine high yield money market accounts, checking services and securities investments and are presently being offered by many large brokerage houses, discount brokers and savings banks. Baron, Martin, "Sorting Through Those Accounts That Do It All," **Los Angeles Times**, February 20, 1983, Part V, p. 1.

5

Stern, Richard L., "Is There Enough Collateral?" **Forbes**, May 9, 1983, pp. 60-61; Darlin, Damon and Daniel Hertzberg, "Annuities Sold by Baldwin Stirring Fears," **The Wall Street Journal**, April 28, 1983, p. 33.

6

The "non-bank" banks, discount brokerage operations of banks, cash management services and many activities of financial service corporations go largely unregulated because their products cross regulatory lines. **CSBS Proceedings, 1983**, (Comments of Congressman Bill McCollum), *supra* note 1; "The Changing Environment for Financial Services and Products," *supra* note 1, at 700; "Homogenization of Financial Institutions: The Legislative and Regulatory Response," *supra* note 1, at 250-255; Woodyard Letter, *supra* note 1, at 4-5.

Because of the lack of definition in the Federal Bank Holding Company Act (18 U.S.C. §1841 et seq.) the bank-like activities (i.e. check cashing services) of credit card services are unregulated. Task Force Staff interview with Keith Ellis, Director of Federal Legislation, Council of State Bank Supervisors, "What's a Bank?" **New York Times**, January 11, 1983, p.30. See also **Board of Trade of the City of Chicago v. Securities and Exchange Commission**, 677 F.2d 1137 (1982).

7

*Supra* note 5; Gilford Securities Incorporated, **Special Situations Research, Baldwin-United Corporation**, (August 17, 1982), (hereinafter, **Gilford Securities Research**); Arkansas Insurance Department, **Report of Financial Examination of the National Investors Life Insurance Company**, Little Rock, Arkansas, as of December 31, 1981, and September 30, 1982, (December 31, 1982), p. 3, (hereinafter, **Arkansas NILIC Report**); Arkansas Insurance Department, **Report of Financial Examination of the National Investors Pension Insurance Company**, Little Rock, Arkansas, as of December 31, 1981, and September 30, 1982, (December 31, 1982), p. 3, (hereinafter, **Arkansas NIPIC Report**); "Baldwin-United Lenders Extend Loans to March 28," **The Wall Street Journal**, March 17, 1983, p. 5; Darlin, Damon, "Baldwin-United Sees Cash Depleted Soon Unless It Gets Financing or Sells Assets," **The Wall Street Journal**, April 19, 1983, p. 2; "Three Butcher Banks Suing Baldwin-United," **American Banker**, April 26, 1983, p. 14; Darlin, Damon, "Baldwin-United Asks Creditors to Extend Debt 'Standstill' Agreement Until September 30," **The Wall Street Journal**, June 13, 1983, p. 6; note 116, *infra*.

8

**Arkansas NILIC Report**, *supra* note 7, at 34; Woodyard Letter, *supra* note 1, at 3-4; Stern, Richard L. and Paul Bornstein, "What Happens When the Music Stops?" **Forbes**, December 20, 1982, pp. 31-33; **Gilford Securities Research**, *supra* note 7, at 3-4; **Gilford Securities Incorporated, Special Situations Update, Baldwin-United Corporation**, (December 7, 1982), pp. 4-7, (hereinafter, **Gilford Securities Update**).



Woodyard Letter, *supra* note 1, at 5-6; NAIC Bell-Budd Report, *supra* note 2; NAIC Model State Insurance Department Funding Bill.

10

The problems of the Arkansas Insurance Department in investigating the NILIC and NIPIC situation provide a case in point. Because of public pressures for balanced government budgets, agencies rarely have enough staff or funds to do as complete a job as possible. William B. Isaac (Chairman of the Federal Deposit Insurance Corporation), C. Todd Conover (Comptroller of the Currency), and S.E.C. Commissioners have called for large increases in staff to be able to continue to regulate as they have. Conte, Christopher, "Regulators Say Banking Safeguards Are Faulty and Need an Overhaul," *The Wall Street Journal*, March 21, 1983, Section 2, p. 1; Hudson, Richard L., "As Stocks Climb, Short-Staffed SEC Tries to Cope With Flood of Securities Offerings," *The Wall Street Journal*, July 25, 1983, p. 13.

11

NAIC Bell-Budd Report, *supra* note 2; COIL Hearing, *supra* note 2; 1982-1983 National Association of State Information Systems Annual Report, Appendix A, (hereinafter, NASIS Annual Report).

12

NASIS Annual Report, *supra* note 11; Serio, Gregory V., "Computers in State Legislatures: The Institution Enters the 20th Century," May, 1983, (unpublished paper, Department of Public Affairs, Nelson A. Rockefeller College of Public Affairs and Policy, State University of New York).

13

The "early warning system" is part of the NAIC Insurance Regulatory Information System (IRIS).

14

McAlear, Charles, "Insurers Can Go Down the Drain," *supra* note 2; COIL Hearing, *supra* note 2, at 14; State of New York, Insurance Department, Regulation of Financial Condition of Insurance Companies, (March, 1974); NAIC Bell-Budd Report, *supra* note 2.

15

*Ibid.*

16

National Bank Act, July 19, 1932, C.508, 47 Stat. 703; Glass-Steagall Act, June 16, 1933, C.614, 49 Stat. 684; Homeowner's Loan Act of 1933, June 13, 1933, C.64, 48 Stat. 132; Securities Act of 1933, May 27, 1933, C.38, 48 Stat. 74; Securities Exchange Act of 1934, June, 1934, C.404, 48 Stat. 881; Robinson-Patman Act, June 9, 1936, C.592, 49 Stat. 1526.

17

Bennett, Robert A., "Inside Citicorp," *New York Times Magazine*, May 29, 1983, p. 15; Adams, John A., "Money Market Mutual Funds: Has Glass-Steagall Been Cracked?" *The Banking Law Journal*, January, 1982, pp. 4-54; Hector, Gary, "The Banks Invade Wall Street," *supra* note 4, at 44; Stern, Richard L. with Laura Saunders, "Brokerage," *Forbes*, January 3, 1983, pp. 87-88; Hershman, Arlene, "The Supercompanies Emerge," *Dun's Business Month*, April, 1983, pp. 44-50; Bennett, Robert A., "Nationwide Banking: Barriers Fall," *New York Times*, June 9, 1983, p. 29; CSBS Proceedings, 1983, *supra* note 1, (statement of Joel Crabtree), at 52, and (statement of Alex Hart), at 59.

National Association of Life Underwriters, **State Legislative Report** (SLR 83-8), February 17, 1983; McLeod, Douglas, "Two States May Let Banks Enter Insurance Business," **Business Insurance**, February 28, 1983, p.2.

In particular, Federal Reserve Board Chairman Paul A. Volcker, Comptroller of the Currency C. Todd Conover and Federal Deposit Insurance Corporation Chairman William M. Isaac disagree sharply on how to approach the mixing of financial institutions. Volcker has called for a legislative moratorium on banking acquisitions by non-banking entities. **U.S. Senate Hearings on the Financial Services Industry**, (statement of Paul A. Volcker), supra note 1. Conover has said that his office will impose a moratorium until January, 1984, but that he will consider applications already filed. **U.S. Senate Hearings on the Financial Services Industry**, (statement of C. Todd Conover), supra note 1. Isaac has called for complete deregulation as soon as possible to let the marketplace impose discipline. **U.S. Senate Hearings on the Financial Services Industry**, (statement of William M. Isaac), supra note 1. "Homogenization of Financial Institutions: The Legislative and Regulatory Response," supra note 1, at 246; Conte, Christopher, "Regulators Say Banking Safeguards are Faulty and Need an Overhaul," supra note 10.

The idea has been broached before and has been generally defeated, mostly because the insurance industry is strongly against it. Alliance of American Insurers, **The New Financial Services**, (1983) at 10; **U.S. Senate Hearings on S.1710 (1977)**, supra note 2.

**U.S. Senate Hearings on S.1710 (1977)**, supra note 2; COIL Hearing, (statement of John K. O'Loughlin), supra note 2, at 9; NAIC Bell-Budd Report, supra note 2.

## Exhibit E

### INTRODUCING REAL COMPETITION INTO PRIVATE PASSENGER CAR INSURANCE

#### (A) NEED TO IMPROVE CURRENT SYSTEM

Regulation has been undermined by Legislation making it less than fully effective.

Thus, it is totally inappropriate to have a cartel setting rates. This is the only industry that does use cartels. Anti-trust Laws don't apply (McCarran-Ferguson).

Yet, movement toward a reliance on competition must assure workable/real competition.

#### (B) BARRIERS TO REAL COMPETITION

- (1) Rate Bureaus influence
- (2) Lack of meaningful Consumer Information
- (3) Mandate on consumers to purchase, no matter what the cost (unbalancing demand/supply equilibrium)
- (4) Anti-Group Laws

#### (C) KEY ELEMENTS NEEDED TO MAKE REAL COMPETITION WORK

Re: (1) \* Abolish North Carolina Rate Bureau.

\* Make other joint rate making activities illegal (avoid ISO).

\* Adopt "little" Anti-Trust Laws, with stiff penalties.

Re: (2) \* Statistics, under uniform statistical plan, to be reported to Commissioner who, through his or her non-industry affiliated contractor, will disseminate same to insurers and the public.

\* Rate and service information will be computerized for public use.

Re: (3) \* The "good driver protection" plan will be continued.

\* Penalties for avoidance (failure to insure promptly).

\* Agent protection.

Re: (4) \* Repeal Anti-Group Laws (if any).

#### RATES

\* Commissioner will establish Facility Rate.

\* Insurers can deviate up or down freely (a transition program should be considered i.e. Legislative cap for 3 years).

\* Customer (in or out of facility) pays the insurer rate.

\* Insurer, if risk reinsured in facility, pays the Facility Rate set by Commissioner to Facility.

\* Simple Classification System.

#### INSOLVENCY PROTECTION - STRENGTHEN GUARANTEE FUNDS/PRE-FUND.

#### (D) CONCLUSION:

This new concept introduces real competition into auto insurance. It is a Bill of Rights for good drivers.





# CAMPAIGN NEWS

Jim Long Election Committee PO Box 10343 Raleigh, NC 27605 919/829-1333

## REMARKS TO THE NORTH CAROLINA GENERAL ASSEMBLY INSURANCE STUDY COMMITTEE

OCTOBER 31, 1984

Mr. Chairmen, Members of the Committee:

Having spent so much of my career on your end of the table--as a legislator or as the Speaker's Counsel--it seems strange to be on this end. It is a privilege to meet with you and to present some of the concerns that I feel this Committee and the Department of Insurance should deal with in the coming years.

I have formed these opinions based on discussions with other regulators, industry and consumer leaders, agents, current Department employees, and--most importantly--thousands of North Carolina citizens with whom I have met in the course of my campaign for Insurance Commissioner--A campaign which has taken me nearly 50,000 miles and all over North Carolina over the past 14 months.

I look forward to working with this Committee and the Legislature in the future to achieve the changes needed in the way this vital product is regulated. As Mr. Hale's earlier presentation highlighted, advances in information and communications technology and the rapid movement toward financial services deregulation clearly portend tremendous changes in the insurance industry--as well as related fields. What distinguishes insurance is that it alone is regulated at the state level.

It is in our State's interest to maintain the regulation of insurance at the State level. State regulation allows more responsiveness to consumers' needs which often differ from state to state. State regulation allows us to tailor regulation to fit local needs rather than being forced into a nationwide uniform scheme. State regulation allows experimentation with new concepts within a state to see if the new concepts are workable. And, we must remember that the most effective, most efficient government is that which is closest to the people.

Prospects for continued State primacy in the regulation of insurance depend directly on the willingness and ability of State officials--legislative and regulatory--to adapt their respective legal and regulatory frameworks and capacities to conform, shape, accommodate, and oversee the tremendous amount of change that has been undergone in this field--and which will dramatically increase even more in the future!

### INSURANCE ISSUES OF THE FUTURE

Mr. Chairmen while there are numerous statutory changes, issues and policy questions that I would like to bring to you today. Hopefully, they will be more appropriate in the coming months and years. However, the focus of today's hearing on financial services deregulation, insurance solvency, and departmental needs is most crucial to the long-term interests of all our citizens. They are also among the most difficult matters which we must face.

In the years ahead, I hope that we can work together on insurance issues that require both new responsibilities and full accountability of the Department of Insurance.

In the move to more competitive insurance markets which have occurred in recent years and continue today, the new responsiveness needed in this changing environment requires that the Insurance Department be able to move quickly...with authority and with purpose. It must have the powers to act! Response time is now limited to prevent a small problem from growing into a large one due to failure to have the powers to act. Consumer protection, company solvency, and product availability depend on this.

### **INSURER SOLVENCY**

The insurance marketplace can function only if there is reasonable assurance that the companies will be able to pay for future losses--in other words company solvency is the primary ingredient to insurance and therefore the most critical task before any commissioner. I view this as the first commandment of consumer protection. The current trend of "cash flow underwriting" in property and casualty is unhealthy.

In health lines both skyrocketing health care costs and the advent of new (and desirable) delivery forms like HMOs, PPOs, and multiple employer trusts pose grave solvency problems. Trends toward offshore captives, third party administrators, and totally unregulated self-insured lines are a form of Russian roulette in the absence of any regulatory oversight. And, the blending and mingling of investment products, their producers, and their marketing poses perhaps our most severe challenge to both insurer solvency and consumer protection.

Specific questions need to be raised with you:

\*Whether our current holding company laws can protect against deliberate bleeding of insurance company reserves? Perhaps stronger penalties are needed for boards of directors (whether of parent company or insurer) who do not recognize their fiduciary and contractual obligations to policy holders as well as (or perhaps before) their obligations to stock holders.

\*Does the current blending of financial and insurance products as well as their producers, suggest new levels of educational, licensing, and registration requirements?

\*Is the existing guaranty fund designed (or even should it be designed) to underwrite questionable products, or products sold in this magnitude. Even if put into effect, it certainly does not provide a very expeditious solution.

\*Are the current regulatory/solvency review standards and tests adequate in this age of electronic funds transmission and new investments?

\*Relatedly, are annual financial statements adequate? Can our State afford to rely solely on the NAIC's current IRIS system and early warning system or on the reports of other departments?

### **INSURANCE DEPARTMENT FISCAL SYSTEMS AND PERSONNEL NEEDS**

What the previous presentations have disclosed to you is that you face the same real challenges in the existing resources, systems and personnel capacities of departments of insurance in the respective states.

While I have not had the chance to completely review changes needed within our Insurance Department, some assessments are obvious.

Exhibit F

## **New Kinds Of Professional Staff Will Be Needed**

As this Committee heard at its last meeting, prior approval and restrictive rate regulation could be replaced by a properly structured and responsive competitive market system of insurance in most lines. To adequately assure that such a system is working and that consumers' interest are provided for, economists, market analysts, antitrust experts, etc. will be required. These will not be cheap and the State will have to compete with private business for these individuals in salary and benefits. Certified actuaries, CPAs, specialized examiners (expert in a particular line and familiar with new products or producers) will be needed in greater numbers.

## **More (Independent) Systems Capacity**

The current project of the computerization of agents licensing and complaint handling is laudable, but it must be viewed for what it is--strictly a streamlining or mechanization of current office work. The real need to serve the interest of the longer range future of our citizens is to develop systems capacity in the examination, assessment, and investment regulation of insurers financial solvencies. Tape to tape annual reports from company to department's computers should be the goal. A Department with the sophistication and equipment to run investment audits, projections, etc. is a must.

## **Greater Collaboration With Other Departments Of Insurance And The NAIC**

This is vital. And will cost money. With direct linkup to the NAIC's audit and warning systems we will be better able to assure our citizens' interest in non-domestic companies. There should be an immediate expansion of our examiners participation in the audits of selected out-of-state insurers!

## **Greater Collaboration With Other Departments And Agencies Within North Carolina Government**

This should be considered. The financial services integration movement may prompt some long-range rethinking of how and where the oversight of other financial institutions should reside in State government. Examination, audit techniques, and systems development might be shared in order to assure more comprehensive oversight as well as economies of scale. Once developed the technical expertise and systems capacity might be utilized by other branches of government in designing or evaluating state employee benefits; risk and insurance programs for state, county, and local officials, and the monitoring of health care cost containment efforts.

## **Increased (And Shared) Reference Sources**

In addition to increasing data systems capacity, current Department policy and reference materials are woefully limited. A major reference center--to be shared with the General Assembly and other departments of government should be developed. This would include at a minimum the insurance statutes and regulations of the 50 states, the federal government, and model NAIC laws.

## **Specific Proposals For Your Consideration**

- 1). Needed staff expansion of the Insurance Department:
  - A) More examiners to conduct audits of companies.
  - B) Computer personnel to handle the data input process and to provide the necessary expertise to develop the required software programs for interfacing with NAIC and companies.
  - C) In-house actuaries, one for property and casualty lines and one for life, accident, and health lines.
  - D) Additional fire and rescue training instructors (recommended by 1984 legislative study committee).
- 2). Expanded computer capabilities:

2). Expanded computer capabilities:

Need to fully and quickly computerize all needed divisions in the Department, particularly the divisions responsible for licensing of agents, handling consumer complaints, auditing of companies, handling fire and casualty filings and handling life, accident, and health filings.

3). A study for recodification of North Carolina's insurance laws:

A) Need a commission with the members appointed by the Senate, the House of Representatives, and the Insurance Commissioner.

B) Set a goal of a review and reworking of laws affecting property and casualty insurance by 1987.

C) A review and reworking of life, accident, and health laws by 1989.

D) Study commission to be jointly staffed by the General Assembly and the Insurance Department.

4). This current Study Committee should immediately begin to address the solvency issues raised here today.

A) Address the computer capabilities of the Department to respond to Phase I, Steps 1, 2, and 3 of the COIL report:

Step 1: Automate state insurance departments to provide the capability to verify promptly mathematical computations and correct information contained in annual reports.

Step 2: Automate state insurance departments to provide the capability to compare annual financial information and the annual IRIS or other early warning system test results with the same data from previous reports and tests.

Step 3: Automate state insurance departments to provide the capability to make projections into the future based on previous annual report information and IRIS or other early warning test results.

B) Endorse concepts of COIL report to process data more quickly with more detailed analysis.

I look forward to working with you in the months and years ahead as we all work on our common goals:

...to provide insurance coverages at affordable rates; and

...to maintain the solvency of companies.

# # #

Exhibit F



## V. Self-Insurers.

1. Any employer desiring to qualify as a self-insurer under the provisions of Section 93 of the Act may make application for this privilege on the forms prescribed by the Commission.

The Commission requires a one-time qualification fee of not less than \$100.00 to accompany any initial application to self-insure. In the case of groups or associations applying to establish a self-insurance program for their members, the \$100.00 fee will be charged to the association making initial application and not to members of the association as they qualify.

Authorization to qualify as an individual self-insurer is based primarily on the financial status and accident experience of the employer applying. Only employers whose modified workers' compensation insurance premium in this State has reached \$100,000.00 a year and whose total fixed assets in North Carolina amount to \$500,000.00 or more will be eligible to apply for individual self-insurer status. For good cause shown, the Commission may waive the requirement on fixed assets or minimum premium volume. The Commission also reserves the right, in its discretion, to revoke any employer's self-insurance privilege, with or without cause, on 10 days notice.

In considering an employer's application to self-insure, and any subsequent annual or semi-annual report or statement filed in connection with that application, special attention shall be given by the Commission to the following factors:

a. The nature and amount of assets, including the proportions which are fixed assets subject to execution in this State.

b. The nature and amount of indebtedness, whether funded or current, secured or unsecured, and whether any defaults exist.

c. Contingent liabilities, if any, including pending litigations or judgments in which the employer is not protected by public liability insurance or other applicable insurance coverage.

## Exhibit G

d. Outstanding compensation claims not covered by insurance.

e. The employer's record of compensable injuries suffered by employees during the preceding three (3) calendar or fiscal years.

f. Normal hazards of the employer's type of business, as shown by applicable compensation manual insurance rates in effect in North Carolina.

g. The relative frequency of death, permanent total disabilities and long-term impairments recorded by the type of business in which the employer is engaged during the preceding three (3) years, as shown by classification of injuries and compensation payments appearing in reports of the Industrial Commission.

An analysis of the foregoing factors does not exclude consideration of any other relevant factors which may affect a particular employer's application, either favorably or unfavorably.

2. All initial applications by individuals or groups must be accompanied by a recent certified audit or certified financial statement.

3. The Commission requires all self-insurers to secure their risk in one of the three following methods:

a. Deposit of acceptable negotiable securities with a minimum current market value of \$200,000.00, reinforced by a \$1,000,000.00 minimum reinsurance policy written by an acceptable company licensed or approved by the Department of Insurance to do business in North Carolina, with the provisions of each policy subject to the approval of the Commission. Such negotiable securities must be accompanied by signed stock or bond powers, unless bearer instruments. If a self-insurer is a corporation, a certified copy of corporate minutes authorizing the corporate officer signing the stock powers to do such in behalf of the corporation will be required. A copy of the reinsurance policy must be filed with the Commission and such contract shall provide an endorsement specifying a written 30-day advance notice

## Exhibit C

of cancellation or modification or refusal to renew to the Commission by the carrier. The continuing adequacy of market value of any such posted securities will be reviewed from time to time. A request for the posting of additional securities to meet minimum market value requirements may be sent to the self-insurer. A new Form 11 will be required in such a circumstance.

b. Execution and filing of a \$200,000.00 surety bond, reinforced by a \$1,000,000.00 minimum reinsurance policy written by an acceptable company licensed or approved by the Department of Insurance to do business in North Carolina, with the provisions of each policy subject to the approval of the Commission. The surety bond shall have no recited termination date and be issued by an acceptable company licensed or approved by the Department of Insurance to do business in North Carolina. The bond must be executed by the proper official of the issuer with currently dated authorizations attached showing such official has power to bind the bonding company. That bond must be countersigned by a local representative of the surety company. The bond must recite an obligation on the part of the issuer to give the Commission a 30-day written notice of intention to cancel. A copy of the reinsurance policy must be filed with the Commission and such contract shall provide an endorsement specifying a written 30-day advance notice of cancellation or modification or refusal to renew to the Commission by the carrier.

c. Deposit with the Commission a negotiable instrument, face value of \$200,000.00 or more, issued by a financial institution incorporated to conduct and conducting business in accordance with Chapter 53 or 54 of the General Statutes of North Carolina, payable on demand to the applicant for self-insurance and the North Carolina Industrial Commission and endorsed by the applicant. This negotiable instrument shall be reinforced by a \$1,000,000.00 minimum reinsurance policy written by an acceptable company licensed or approved by the Department of Insurance to do business in North Carolina, with the provisions of each policy subject to the approval of the Commission. A copy of the reinsurance policy must be filed with the Commission and such contract shall provide an endorsement



## Exhibit G

specifying a written 30-day advance notice to the Commission of cancellation, modification or refusal to renew. If the applicant is a corporation, a certified copy of corporate minutes authorizing the corporate officer signing such endorsement to do such in behalf of the corporation must accompany the application. Also with the application must be a notarized statement by an officer of the issuing corporation that the deposits of that corporation are insured by the Federal Deposit Insurance Corporation, the Federal Savings and Loan Insurance Corporation or the North Carolina Savings Guaranty Corporation, and that the North Carolina Industrial Commission will be told in writing should there be any change in the insured status of deposits of the issuing corporation.

4. The Commission requires self-insured groups or associations to execute a surety bond of \$1,000,000.00, or deposit a negotiable instrument in this amount of the type described in 3c above or satisfy the formula of \$20,000.00 bond per member to a maximum of \$400,000.00 and obtain reinsurance to cover the remainder of the required surety in the amount of \$1,000,000.00. The provisions of each reinsurance policy shall be subject to the Commission's approval. The surety bond and reinsurance policy must be issued by an acceptable company licensed or approved to do business in North Carolina and must carry a written obligation to give the Industrial Commission 30 days written notice of intention to modify, cancel or refuse to renew.

Self-insured groups or associations are also required to file with the Commission an indemnity agreement between its members binding the group or association and each member thereof, jointly and severally, to comply with the provisions of the Workers' Compensation Act. This indemnity agreement, signed by each member, must be filed with each application before the application can be approved. Withdrawal from such a group or association automatically terminates a member's self-insured status and that employer must either purchase workers' compensation insurance coverage or qualify as an individual self-insurer.

## Exhibit G

5. Every employer, now qualified as or desiring to become a self-insurer, must, unless good cause be shown for exemption, designate an office in the State of North Carolina for the handling of claims. Service organizations handling claims for self-insurance under the rules of this Commission shall establish an office in this State for the handling of claims. Every office designated or established shall be staffed during normal working hours and be available for immediate telephone contact with the Commission and the public. During normal working hours at this office at least one staff member shall be authorized to execute instruments for the payment of compensation.

6. After a company has satisfactorily completed the requirements stated above and has been approved for self-insurer status, there will be issued a certificate of compliance which will remain in force subject to cancellation at the discretion of the Commission. The effective date to qualify may not be backdated.

7. Revision in the amount of surety required may be made by the Industrial Commission should the Commission deem such to be necessary. Such revision shall be complied with by the self-insurer within 30 days from receipt of notice of revision.

8. Self-insurer forms, as adopted by the Commission, must be completed for initial qualification. These forms will not have to be filed annually, but must be resubmitted when any of the following changes occur:

a. Change in the name of employer or in corporate structure of the employer.

b. Any change in the required amount of bond.

c. Any change in the securities on deposit with the State Treasurer.

9. The Commission requires self-insurers to file each year certified annual financial reports and a list of corporate officers and directors. A \$20.00 review fee will be billed

## Exhibit G

annually to cover the administrative costs of reviewing these reports and the cost of claims forms. These reports must be filed at the end of each self-insurer's fiscal year so that the most current financial information is available to the Commission.

10. Payroll reports of all self-insurers must be submitted on the proper forms no later than January 31 for the preceding calendar year. Self-insurer taxes are based on payroll and employers are billed annually at a rate of 1.6% of the normal compensation premium for companies domesticated in the State and 4% for foreign corporations. Taxes are due and payable not later than April 14th of the year in which they are billed. A late payment penalty of 10% of the unpaid balance will be charged plus  $1/2$  of 1% interest per month on the unpaid balance until paid. A fraction of a month will be counted as a whole month.

11. The records of the Commission insofar as they relate to self-insurers shall not be open to the public, but only to parties satisfying the Commission of their right to inspect them.

The effective date of this rule is January 1, 1983.

INTRODUCED BY:

Referred to:

A BILL TO BE ENTITLED

AN ACT TO TRANSFER THE REGULATION OF WORKERS' COMPENSATION  
SELF-INSURANCE FROM THE INDUSTRIAL COMMISSION TO THE  
DEPARTMENT OF INSURANCE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 97-93 is rewritten to read:

"§ 97-93. Employers required to carry insurance or  
prove financial ability to pay for benefits; self-insured  
employers regulated by Commissioner of Insurance.--(a)

Every employer subject to the provisions of this Article  
relative to the payment of compensation shall either:

- (1) Insure and keep insured his liability under this  
Article in any authorized corporation, asso-  
ciation, organization, or in any mutual insurance  
association formed by a group of employers so  
authorized; or
- (2) Furnish to the Commissioner of Insurance  
satisfactory proof of the employer's financial  
ability, either alone or through membership in a  
group comprising two or more employers who agree to  
pool their liabilities under this Article, to direct-  
ly pay the compensation in the amount and manner and  
when due as provided for in this Article.

1 (b) In the case of subdivision (a) (2) of this section,  
2 the Commissioner of Insurance may require the deposit of an  
3 acceptable security, indemnity, or bond to secure the  
4 payment of compensation liabilities as they are incurred.  
5 Any individual employer or group of employers who furnish  
6 proof of financial ability under subdivision (a) (2) of this  
7 section shall be governed in all respects by this Article  
8 and by such rules as may be promulgated by the Commissioner  
9 of Insurance.

10 (c) Payment of dividends to the members of any group  
11 of employers who agree to pool their liabilities under  
12 subdivision (a) (2) of this section shall not be contingent  
13 upon the maintenance or continuance of membership in such  
14 pools."

15 Sec. 2. G.S. 97-100(j) is amended in the second,  
16 third, and fifth lines by substituting the words, "Commis-  
17 sioner of Insurance" for the word, "Commission."

18 Sec. 3. G.S. 105-228.7 is amended in the final  
19 paragraph by rewriting the fourth and fifth lines to read:

20 "Insurance Commissioner as provided in G.S. 97-100(j)."

21 Sec. 4. This act shall become effective July 1,  
22 1985.



INTRODUCED BY:

Referred to:

1                               A BILL TO BE ENTITLED  
2       AN ACT TO CREATE A COMMISSION TO STUDY THE GENERAL STATUTES  
3               OF NORTH CAROLINA PERTAINING TO THE REGULATION OF  
4               INSURANCE.

5       The General Assembly of North Carolina enacts:

6                       Section 1.   The General Assembly finds and de-  
7       clares that:

8               (a)   The North Carolina Commissioner and Department of  
9       Insurance are charged by statute with the responsibility of  
10      oversight and regulation of insurance companies, asso-  
11      ciations, agents, and rating organizations that are under  
12      the jurisdiction of the State of North Carolina.

13              (b)   The Commissioner and Department of Insurance have  
14      responsibilities to promulgate rules to effectively adminis-  
15      ter the insurance statutes and fairly regulate the business  
16      of insurance in North Carolina.

17              (c)   The scope of the responsibilities of the Commis-  
18      sioner and Department of Insurance has grown significantly  
19      in recent years.

20              (d)   There have been problems in the construction,  
21      interpretation, and understanding of the insurance statutes  
22      of this State, many of which have been described by the  
23      Supreme Court of North Carolina as "confusing and unwieldy."  
24

1                   Sec. 2. There is created the North Carolina  
2 Insurance Regulation Study Commission, hereinafter referred  
3 to as the Commission. The Commission shall consist of  
4 twelve members, appointed as follows:

5           (a) The Commissioner of Insurance shall appoint four  
6 members; two of which shall be members of the general  
7 public, one of which shall be a property and casualty  
8 insurance agent duly licensed by the State of North  
9 Carolina, and one of which shall be a representative of a  
10 property and casualty insurer duly licensed to transact the  
11 business of insurance in this State.

12           (b) The Speaker of the House shall appoint four  
13 members; three of which shall be members of the North  
14 Carolina House of Representatives, and one of which shall be  
15 a property and casualty insurance agent duly licensed by the  
16 State of North Carolina, who may also be a member of the  
17 North Carolina House of Representatives.

18           (c) The President of the Senate shall appoint four  
19 members; three of which shall be members of the North  
20 Carolina Senate, and one of which shall be a representative  
21 of a property and casualty insurer duly licensed to transact  
22 the business of insurance in this State, who may also be a  
23 member of the North Carolina Senate.

24 In the event of any vacancy, the appropriate appointing  
25 authority shall appoint a replacement to serve the remainder  
26 of the unexpired term. Legislative members of the Commis-  
27 sion shall be paid subsistence and mileage allowances  
28 authorized by G.S. 120-3.1 for services on the Commission



1 when the General Assembly is not in session. Other members  
2 of the Commission shall be paid the per diem and allowances  
3 authorized by G.S. 138-5. The Commission shall elect a  
4 chairman and vice-chairman from its membership.

5 Sec. 3. The Commission is authorized to review  
6 and analyze:

7 (a) The various systems or methods of property and  
8 liability insurance regulation in this State and in other  
9 states, including the licensing of insurers, agents, brok-  
10 ers, and adjusters; regulation of premium rates, policy  
11 forms, and classifications; financial regulation of insur-  
12 ers; residual and substandard insurance markets; and the  
13 impact on the property and liability insurance market caused  
14 by the integration of the components of the financial  
15 services industry: banking, securities, and insurance.

16 (b) The form, style, and intelligibility of the North  
17 Carolina General Statutes concerning property and liability  
18 insurance and the manners in which such statutes can be  
19 rewritten and recodified to improve them in this regard.

20 Sec. 4. The Commission may meet in the State  
21 Legislative Building or Legislative Office Building and  
22 utilize the services of the staffs of the Legislative  
23 Services Office and the Department of Insurance. The  
24 Commission may also employ additional clerical and profes-  
25 sional staff in carrying out the provisions of this act.

26 Sec. 5. The Commission is authorized to submit an  
27 interim report to the 1985 General Assembly, Regular Session  
28 1986 on its convening date. Such interim report may relate

1 only to budgetary matters of the Department of Insurance or  
2 of the Commission. The Commission shall submit its final  
3 report to the 1987 General Assembly on its convening date.

4 Sec. 6. There is appropriated from the General  
5 Fund to the Commission for fiscal years 1985-86 and 1986-87  
6 the total sum of fifty thousand dollars (\$50,000) to carry  
7 out the provisions of this act. Any unused funds shall  
8 revert to the General Fund at the end of fiscal year  
9 1986-87.

10 Sec. 7. This act shall become effective July 1,  
11 1985.



